

OPEN MEETING ITEM

11/17/16



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COMMISSIONERS
DOUG LITTLE - Chairman
BOB STUMP
BOB BURNS
TOM FORESE
ANDY TOBIN

JODI JERICH
EXECUTIVE DIRECTOR



DIRECTOR
SECURITIES DIVISION
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ORIGINAL

ARIZONA CORPORATION COMMISSION

MEMORANDUM

TO: Doug Little - Chairman
Bob Stump
Bob Burns
Tom Forese
Andy Tobin

Arizona Corporation Commission

DOCKETED

NOV 03 2016

FROM: Matthew J. Neubert *MJN*
Director of Securities

DOCKETED BY

JB

DATE: November 3, 2016

RE: Proposed Order to Cease and Desist, Order of Revocation, Order of Denial, Order for Administrative Penalties and Consent to Same by David J. Escarcega, Docket No. S-20956A-16-0090

CC: Jodi Jerich, Executive Director

Please find attached a proposed Order to Cease and Desist, Order of Revocation, Order of Denial, Order for Administrative Penalties and Consent to Same ("Consent Order") by David J. Escarcega.

Between February 2012 and June 2013, Mr. Escarcega violated the Securities Act and the Investment Management Act by the manner in which he sold registered debentures (corporate debt securities) of a life settlement company. Mr. Escarcega was a registered securities salesman and the debentures were an approved product of his dealer. Mr. Escarcega sold approximately \$4,144,000 of the debentures to forty-seven investors.

In selling the debentures, Mr. Escarcega misrepresented to some of the investors that the debentures involved minimal risk, that they could be freely liquidated, or that they provided guaranteed interest, income, rate of return, or a guarantee against market losses. He also engaged in dishonest and unethical practices in the securities industry, including recommending the debentures to investors for whom they were not suitable, conducting sales presentations that were misleading about how risky the debentures were, and instructing investors to sign and date blank forms that he said he would fill in later.

The proposed Consent Order requires Mr. Escarcega to permanently cease and desist from violating the Securities Act and the Investment Management Act; revokes his salesman registration; denies his application for an investment advisor license; and requires him to pay an administrative penalty in the amount of \$100,000. The proposed Consent Order does not include an order of restitution as the investments are currently paying interest as required by the debentures.

The Securities Division believes the proposed Consent Order is appropriate to protect the public welfare.

Originator: Paul Kitchen

1 **BEFORE THE ARIZONA CORPORATION COMMISSION**

2 **COMMISSIONERS**

3 DOUG LITTLE - Chairman
4 BOB STUMP
5 BOB BURNS
6 TOM FORESE
ANDY TOBIN

7 In the matter of:

8 David J. Escarcega (CRD no. 4367584), an
unmarried man,

9 Respondent.

DOCKET NO. S-20956A-16-0090

10 DECISION NO. _____

11 **ORDER TO CEASE AND DESIST, ORDER**
12 **OF REVOCATION, ORDER OF DENIAL,**
13 **ORDER FOR ADMINISTRATIVE**
14 **PENALTIES AND CONSENT TO SAME**
15 **BY: RESPONDENT DAVID J. ESCARCEGA**

16 Respondent David J. Escarcega ("Respondent") elects to permanently waive any right to a
17 hearing and appeal under Articles 11 and 12 of the Securities Act of Arizona, A.R.S. § 44-1801 *et*
18 *seq.* ("Securities Act") and Articles 7 and 8 of the Arizona Investment Management Act, A.R.S. §
19 44-3101 *et seq.* ("Investment Management Act") with respect to this Order to Cease and Desist,
20 Order of Revocation, Order of Denial, Order for Administrative Penalties and Consent to Same
21 ("Order"). Respondent admits the jurisdiction of the Arizona Corporation Commission
22 ("Commission"); and solely for purposes of this proceeding and any other proceeding in which the
23 Commission is a party, neither admits nor denies the Findings of Fact and Conclusions of Law
24 contained in this Order; and consents to the entry of this Order by the Commission.

25 **I.**

26 **FINDINGS OF FACT**

1. David J. Escarcega ("Escarcega") was an Arizona resident at all relevant times, and he
has been an unmarried man since 2012.

1 2. From April 12, 2010, to September 13, 2013, and from September 17, 2013, to April 5,
2 2016, Escarcega was registered by the Commission as a securities salesman with CRD no. 4367584,
3 and employed by registered securities dealer Center Street Securities, Inc. (CRD no. 26898) ("Dealer").

4 3. On December 19, 2014, Escarcega filed an application with the Commission for
5 licensure as an investment advisor representative for Center Street Advisors, Inc. (CRD no. 169329).

6 4. In 2012, Escarcega's securities Dealer approved a new securities product for sale. The
7 product was a debenture ("Debenture") issued by the parent company of a life settlement company,
8 a company in the business of purchasing life insurance policies, servicing the policies, and collecting
9 the death benefits.

10 5. The Debentures were registered by the Commission as a special registration pursuant
11 to A.R.S. § 44-1845(B)(1). This special registration imposed specific suitability requirements
12 pursuant to A.A.C. R14-4-144(C) on sales of the Debentures within Arizona. Specifically, A.A.C.
13 R14-4-144(C) requires that the securities dealer have a reasonable belief that each investor has a
14 minimum net worth of \$350,000, or \$400,000 when combined with spouse, exclusive of home, home
15 furnishings, and automobiles ("relevant net worth"), and the investment must not exceed 10% of the
16 relevant net worth. Alternatively, the securities dealer must have a reasonable belief that the investor
17 had a minimum gross income in the prior year of \$150,000, or \$200,000 when combined with spouse,
18 and a reasonable expectation that the investor will have such income in the present year.

19 6. The documents Escarcega submitted to Dealer for the purchase of Debentures by the
20 Arizona investors identified below did not reflect any gross income over \$150,000 or \$200,000 when
21 combined with spouse.

22 7. The Debentures were a speculative investment involving a high degree of risk,
23 including the risk of losing the entire investment. The Debentures were illiquid and not suitable for
24 investors that had any need for liquidity before the maturity date. The Debentures were not listed on
25 any exchange. Although the issuer voluntarily redeemed some Debentures early, investors had no
26

1 right to require the issuer to redeem the Debentures before their maturity date except in cases of
2 death, bankruptcy, or total disability.

3 8. From 2012 to 2014, Escarcega sold Debentures to 47 investors.

4 9. For investors who purchased Debentures from him, Escarcega prepared an account
5 application describing their approximate income and assets and their general investment objectives.
6 Escarcega also prepared a suitability form describing in more detail their income, assets, and the
7 percentage of their net worth to be invested in the Debenture. The suitability form also characterized
8 their investment objectives. The account applications and suitability forms categorized investment
9 objectives on the same scale of five categories: income, balanced/conservative growth, growth,
10 aggressive growth, or speculation.

11 10. Escarcega also prepared a switch letter for some investors, which was a form required
12 if the investor had liquidated, redeemed, or exchanged another investment within 30 days before
13 purchasing a Debenture.

14 11. Married Arizona residents J.B. and D.B. invested \$117,000 in a Debenture through
15 Escarcega, representing over 29% of their relevant net worth and exceeding Arizona's 10%
16 suitability limit. These investors could not have afforded to lose their entire \$117,000 Debenture
17 investment. Escarcega misrepresented to them that the Debenture interest payments were guaranteed
18 and that the Debenture investment was safe. Escarcega also misrepresented to Dealer on the
19 suitability form he prepared that the investors had a \$635,000 net worth, including bonds and mutual
20 funds. Their actual net worth was less than \$400,000, and they did not own any bonds or mutual
21 funds.

22 12. Arizona resident P.B. invested \$103,000 in a Debenture through Escarcega,
23 representing at least 17% of his relevant net worth and exceeding Arizona's 10% suitability limit.
24 This investor could not have afforded to lose his entire \$103,000 Debenture investment. Escarcega
25 misrepresented to him that the Debenture was guaranteed against market losses.
26

1 13. Arizona resident R.L. invested \$99,000 in a Debenture through Escarcega,
2 representing at least 16% of his relevant net worth and exceeding Arizona's 10% suitability limit.
3 This investor could not have afforded to lose his entire \$99,000 Debenture investment. Although the
4 Debentures were a speculative investment involving a high degree of risk, the investor's account
5 application and suitability form indicated that his investment objectives were in the most conservative
6 category. Escarcega repeatedly misrepresented to the investor that the Debenture investment
7 involved minimal risk and also misrepresented that the investor could liquidate the Debenture at any
8 time. Escarcega also instructed this investor to sign blank forms for his Debenture investment that
9 Escarcega completed later.

10 14. Arizona resident K.L.K. invested \$65,500 in a Debenture through Escarcega,
11 representing at least 22% of his relevant net worth and exceeding Arizona's 10% suitability limit.
12 This investor could not have afforded to lose his entire \$65,500 Debenture investment. Escarcega
13 misrepresented to the investor that he could liquidate his Debenture investment at any time. As part
14 of the investor's application, Escarcega had him sign and date a blank switch letter that Escarcega
15 intended to complete later.

16 15. Arizona resident R.E. invested \$67,000 in a Debenture through Escarcega.
17 Escarcega's handwritten notes on the investor's switch letter misrepresented to the investor that the
18 Debenture would provide a "guaranteed income stream."

19 16. California residents N.J. and R.J. invested \$52,875.23 in a Debenture through
20 Escarcega. Escarcega's handwritten notes on the investors' switch letter misrepresented to the
21 investors that the Debenture would provide "guaranteed interest."

22 17. California resident C.M. invested \$117,000 in a Debenture through Escarcega.
23 Escarcega's handwritten notes on the investor's switch letter misrepresented to her that the Debenture
24 would "maximize ... liquidity" compared to her longer term but redeemable fixed annuity.
25
26

1 18. California resident N.Z. invested in two Debentures through Escarcega totaling
2 \$64,500. Escarcega's handwritten notes on the investor's switch letters misrepresented to her that the
3 Debentures would provide a "guaranteed rate of return" unlike her fixed indexed annuity.

4 19. Married Arizona residents D.K. and K.K. invested in four Debentures through
5 Escarcega totaling \$500,000, representing at least 28% of their relevant net worth and exceeding
6 Arizona's 10% suitability limit.

7 20. Arizona resident N.H. invested \$329,500 in a Debenture through Escarcega,
8 representing at least 28% of her relevant net worth and exceeding Arizona's 10% suitability limit.

9 21. Arizona resident P.A.B. invested in two Debentures through Escarcega totaling
10 \$267,000, representing at least 26% of her relevant net worth and exceeding Arizona's 10%
11 suitability limit.

12 22. Arizona resident S.C. invested \$78,000 in a Debenture through Escarcega,
13 representing at least 15% of her relevant net worth and exceeding Arizona's 10% suitability limit.

14 23. Arizona resident M.D. invested in two Debentures through Escarcega totaling
15 \$111,000, representing at least 13% of his relevant net worth and exceeding Arizona's 10%
16 suitability limit.

17 24. Arizona resident A.M. invested \$87,000 in a Debenture through Escarcega,
18 representing at least 12% of his relevant net worth and exceeding Arizona's 10% suitability limit.

19 25. Although the investors were fortunate, and the Debentures have performed adequately
20 so far, Escarcega's unsuitable Debenture sales improperly exposed investors to the risk of
21 catastrophic losses.

22 26. For Arizona investors who exceeded the 10% of net worth suitability limit, the issuer
23 of the Debentures subsequently partially refunded principal to those investors to bring them within
24 the suitability limit based on the net worth listed on their suitability forms.

25 27. California resident N.G. invested \$25,000 in a Debenture through Escarcega.
26 Escarcega did not tell her about the risks of the Debentures, and his seminar falsely implied that they

1 were low risk. She told Escarcega that she wanted a secure investment with no risk, and she believed
2 the Debentures were very low risk.

3 28. California residents W.J. and S.M. invested in two Debentures through Escarcega
4 totaling \$156,300. As part of the investors' application, Escarcega had them sign and date a blank
5 switch letter that Escarcega intended to complete later.

6 29. Escarcega also had investors R.L. and K.L.K sign and date blank forms, as alleged in
7 paragraphs 16 and 17, above.

8 30. Escarcega falsified data on a Debenture suitability form for investors J.B. and D.B.,
9 as alleged in paragraphs 14, above.

10 31. Escarcega told his customers that the Debentures involved some risk factors, but he
11 did not tell any of his customers that the Debentures involved a high degree of risk. The prospectus
12 and other written materials disclosed the Debentures' illiquidity, degree of risk, and other risk factors.

13 II.

14 CONCLUSIONS OF LAW

15 1. The Commission has jurisdiction over this matter pursuant to Article XV of the
16 Arizona Constitution, the Securities Act, and the Investment Management Act.

17 2. Respondent violated A.R.S. § 44-1991.

18 3. Respondent's conduct subjects Respondent to an order of revocation pursuant to
19 A.R.S. §§ 44-1962(A)(2) and (A)(10).

20 4. Respondent's conduct subjects Respondent to an order of denial pursuant to A.R.S.
21 § 44-3201(A)(13).

22 5. Respondent's conduct is grounds for a cease and desist order pursuant to A.R.S. § 44-
23 2032 and A.R.S. § 44-1962.

24 6. Respondent's conduct is grounds for administrative penalties under A.R.S. § 44-2036
25 and A.R.S. § 44-1962.

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3 **III.**4 **ORDER**

5 THEREFORE, on the basis of the Findings of Fact, Conclusions of Law, and Respondent's
6 consent to the entry of this Order, attached and incorporated by reference, the Commission finds that
7 the following relief is appropriate, in the public interest, and necessary for the protection of investors:

8 IT IS ORDERED, pursuant to A.R.S. § 44-2032, that Respondent, and any of Respondent's
9 agents, employees, successors and assigns, permanently cease and desist from violating the Securities
10 Act.

11 IT IS FURTHER ORDERED that Respondent complies with the attached Consent to Entry
12 of Order.

13 IT IS FURTHER ORDERED, pursuant to A.R.S. § 44-2036 and A.R.S. § 44-1962, that
14 Respondent shall pay an administrative penalty in the amount of \$100,000 as a result of the conduct
15 set forth in the Findings of Fact and Conclusions of Law. Payment shall be due upon entry of this
16 Order. Payment shall be payable to the "State of Arizona." Any amount outstanding shall accrue
17 interest at the rate of 4.5 percent per annum.

18 IT IS FURTHER ORDERED, pursuant to A.R.S. § 44-1962, that Respondent's securities
19 salesman registration is revoked.

20 IT IS FURTHER ORDERED, pursuant to A.R.S. § 44-3201, that Respondent's application
21 for licensure as an investment adviser is denied.

22 For purposes of this Order, a bankruptcy filing by Respondent shall be an act of default. If
23 Respondent does not comply with this Order, any outstanding balance may be deemed in default and
24 shall be immediately due and payable.

25 IT IS FURTHER ORDERED, that if Respondent fails to comply with this order, the
26 Commission may bring further legal proceedings against Respondent, including application to the
superior court for an order of contempt.

1 IT IS FURTHER ORDERED, that no finding of fact or conclusion of law contained in this
2 Order shall be deemed binding against any Respondent under this Docket Number who has not
3 consented to the entry of this Order.

4 IT IS FURTHER ORDERED that this Order shall become effective immediately.

5
6 BY ORDER OF THE ARIZONA CORPORATION COMMISSION

7
8 _____
CHAIRMAN LITTLE

COMMISSIONER STUMP

9
10 _____
11 COMMISSIONER FORESE COMMISSIONER TOBIN COMMISSIONER BURNS

12
13 IN WITNESS WHEREOF, I, JODI A. JERICH, Executive
14 Director of the Arizona Corporation Commission, have
15 hereunto set my hand and caused the official seal of the
16 Commission to be affixed at the Capitol, in the City of Phoenix,
17 this _____ day of _____, 2016.

18 _____
JODI A. JERICH
19 EXECUTIVE DIRECTOR

20 _____
DISSENT

21
22 _____
23 DISSENT

24 This document is available in alternative formats by contacting Shaylin A. Bernal, ADA
25 Coordinator, voice phone number 602-542-3931, e-mail sabernal@azcc.gov.

26 (PSK)

CONSENT TO ENTRY OF ORDER

1
2 1. Respondent David J. Escarcega ("Respondent"), an individual, admits the jurisdiction
3 of the Commission over the subject matter of this proceeding. Respondent acknowledges that
4 Respondent has been fully advised of Respondent's right to a hearing to present evidence and call
5 witnesses and Respondent knowingly and voluntarily waives any and all rights to a hearing before
6 the Commission and all other rights otherwise available under Article 11 of the Securities Act, Article
7 7 of the Investment Management Act, and Title 14 of the Arizona Administrative Code. Respondent
8 acknowledges that this Order to Cease and Desist, Order of Revocation, Order of Denial, Order for
9 Administrative Penalties and Consent to Same ("Order") constitutes a valid final order of the
10 Commission.

11 2. Respondent knowingly and voluntarily waives any right under Article 12 of the
12 Securities Act and Article 8 of the Investment Management Act to judicial review by any court by
13 way of suit, appeal, or extraordinary relief resulting from the entry of this Order.

14 3. Respondent acknowledges and agrees that this Order is entered into freely and
15 voluntarily and that no promise was made or coercion used to induce such entry.

16 4. Respondent acknowledges that Respondent has been represented by an attorney in
17 this matter, Respondent has reviewed this Order with Respondent's attorneys, Paul Roshka and Craig
18 M. Waugh, and understands all terms it contains.

19 5. Respondent neither admits nor denies, and only for purposes of this proceeding and
20 any other proceeding in which the Commission is a party, the Findings of Fact and Conclusions of
21 Law contained in this Order; however, if the Commission is a party to the matter, including this case,
22 agrees he does not dispute, the Findings of Fact and Conclusions of Law contained in this Order; and
23 consents to the entry of this Order by the Commission. Respondent agrees that Respondent shall not
24 contest the validity of the Findings of Fact and Conclusions of Law contained in this Order in any
25 present or future proceeding in which the Commission is a party.
26

1 6. Respondent further agrees that he shall not deny or contest the Findings of Fact and
2 Conclusions of Law contained in this Order in any present or future: (a) bankruptcy proceeding, or
3 (b) non-criminal proceeding in which the Commission is a party (collectively, "Proceeding(s)").
4 They further agree that in any such Proceedings, the Findings of Fact and Conclusions of Law
5 contained in this Order may be taken as true and correct and that this Order shall collaterally estop
6 them from re-litigating with the Commission or any other state agency, in any forum, the accuracy
7 of the Findings of Fact and Conclusions of Law contained in this Order. In the event Respondent
8 pursues bankruptcy protection in the future, he further agrees that in such bankruptcy proceeding,
9 pursuant to 11 U.S.C. § 523(a)(19), the following circumstances exist:

10 A. The obligations incurred as a result of this Order are a result of the conduct set forth
11 in the Findings of Fact and Conclusions of Law in the Order and are for the violation of Arizona
12 state securities laws, pursuant to 11 U.S.C. § 523(a)(19)(A)(i);

13 B. This Order constitutes a judgment, order, consent order, or decree entered in a state
14 proceeding pursuant to 11 U.S.C. § 523(a)(19)(B)(i), a settlement agreement entered into by
15 Respondent pursuant to 11 U.S.C. § 523(a)(19)(B)(ii), and a court order for damages, fine, penalty,
16 citation, restitution payment, disgorgement payment, attorney fee, cost or other payment owed by
17 Respondent pursuant to 11 U.S.C. § 523(a)(19)(B)(iii).

18 7. By consenting to the entry of this Order, Respondent agrees not to take any action or
19 to make, or permit to be made, any public statement denying, directly or indirectly, any Finding of
20 Fact or Conclusion of Law in this Order or creating the impression that this Order is without factual
21 basis.

22 8. While this Order settles this administrative matter between Respondent and the
23 Commission, Respondent understands that this Order does not preclude the Commission from
24 instituting other administrative or civil proceedings based on violations that are not addressed by this
25 Order.
26

1 9. Respondent understands that this Order does not preclude the Commission from
2 referring this matter to any governmental agency for administrative, civil, or criminal proceedings
3 that may be related to the matters addressed by this Order.

4 10. Respondent understands that this Order does not preclude any other agency or officer
5 of the state of Arizona or its subdivisions from instituting administrative, civil, or criminal
6 proceedings that may be related to matters addressed by this Order.

7 11. Respondent agrees that Respondent will not apply to the state of Arizona for
8 registration as a securities dealer or salesman or for licensure as an investment adviser or investment
9 adviser representative until such time as all penalties under this Order are paid in full.

10 12. Respondent agrees that Respondent will not exercise any control over any entity that
11 offers or sells securities or provides investment advisory services within or from Arizona until such
12 time as all restitution and penalties under this Order are paid in full.

13 13. Respondent agrees that Respondent will continue to cooperate with the Securities
14 Division including, but not limited to, providing complete and accurate testimony at any hearing in
15 this matter and cooperating with the state of Arizona in any related investigation or any other matters
16 arising from the activities described in this Order.

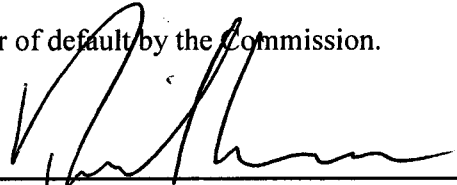
17 14. Respondent consents to the entry of this Order and agrees to be fully bound by its
18 terms and conditions.

19 15. Respondent acknowledges and understands that if Respondent fails to comply with
20 the provisions of the order and this consent, the Commission may bring further legal proceedings
21 against Respondent, including application to the superior court for an order of contempt.

22 16. Respondent understands that default shall render Respondent liable to the
23 Commission for its costs of collection, including reasonable attorneys' fees and interest at the
24 maximum legal rate.


25 17. Respondent agrees and understands that if Respondent fails to make any payment as
26 required in the Order, any outstanding balance shall be in default and shall be immediately due and

1 payable without notice or demand. Respondent agrees and understands that acceptance of any partial
2 or late payment by the Commission is not a waiver of default by the Commission.

3
4 
5 (David J. Escarcega)

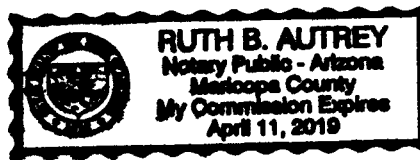
6 STATE OF ARIZONA)
7) ss
8 County of)

9 SUBSCRIBED AND SWORN TO BEFORE me this 2nd day of November.

10
11 
12 NOTARY PUBLIC

12 My commission expires:

13 4-11-19.



SERVICE LIST FOR: David J. Escarcega (CRD no. 4367584)

Paul J. Roshka, Jr.
Craig Waugh
POLSINELLI, P.C.
One East Washington St., Suite 1200
Phoenix, AZ 85004-2568
Attorneys for Respondent

1 **BEFORE THE ARIZONA CORPORATION COMMISSION**

2
3 COMMISSIONERS

4 DOUG LITTLE – Chairman
5 BOB STUMP
6 BOB BURNS
TOM FORESE
ANDY TOBIN

7 In the matter of:)

DOCKET NO. S-20956A-16-0090

8 David J. Escarcega (CRD no. 4367584), an)
9 unmarried man,)

**NOTICE OF FILING OF PROPOSED
OPEN MEETING AGENDA ITEM**

10 Respondent.)

11 On this 3rd day of November, 2016, the foregoing document was filed with Docket Control
12 as a Securities Division Memorandum & Proposed Order, and copies of the foregoing were mailed
13 on behalf of the Securities Division to the following who have not consented to email service. On
14 this date or as soon as possible thereafter, the Commission's eDocket program will automatically
15 email a link to the foregoing to the following who have consented to email service.

16
17
18 Paul J. Roshka, Jr.
19 Craig Waugh
20 POLSINELLI, P.C.
One East Washington St., Suite 1200
Phoenix, AZ 85004-2568
Attorneys for Respondent

21
22
23 By: 

24
25
26
Decision No. _____